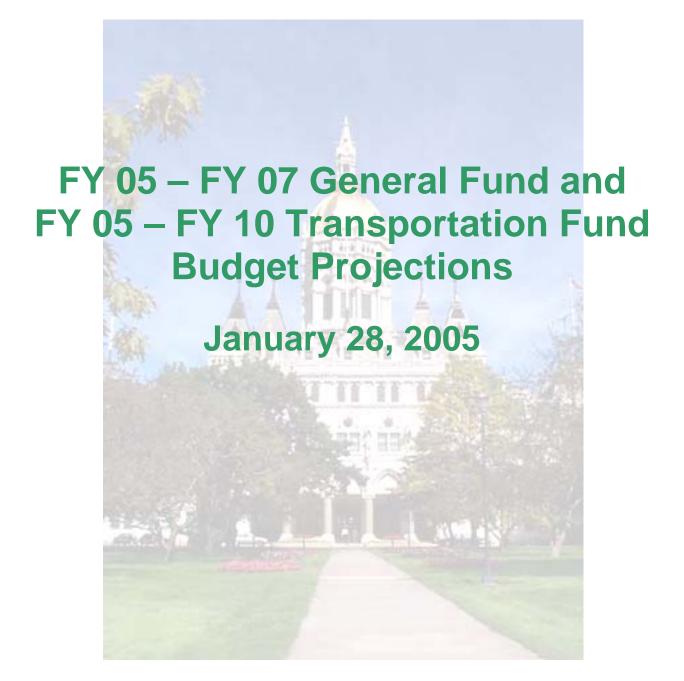
Connecticut General Assembly office of fiscal analysis



Report Highlights

- FY 05 General Fund surplus is projected at \$369.2 million (\$118.2 million higher than estimated on 11/12/04). See pages 1 7 for details.
- General Fund current services deficits are projected for FY 06 (\$672.6 million) and FY 07 (\$859.6 million). These projections are higher than the amounts estimated on 11/12/04 by \$68.8 million in FY 06 and \$158.2 million in FY 07. See pages 22 23 for details.
- FY 05 Transportation Fund operating deficit is projected at \$2.3 million (\$5.4 million less than estimated on 11/12/04), which reduces the cumulative surplus from \$132.1 (un-audited) to \$129.9 million. The lowered deficit projection reflects the Governor's statewide hiring freeze announcement, increased snow and ice removal costs and reduced debt service. See pages 24 28 for details.
- Out year projections indicate that the Transportation Fund will continue to experience operating deficits each year, which will completely eliminate the cumulative surplus in FY 09. This is attributable to the combined effects of growth rates in expenditures accelerating faster than the anticipated growth in revenues.

Preliminary General Fund Budget Projections FY 05, FY 06 and FY 07 as of January 28, 2005

	FY 04			FY 05]	FY 06	FY 07
Budget Overview:	Surplus Estimate <u>FY 04</u>		OFA Estimate as of Budget Passage 4/29/04 FY 05	OFA Estimate as of Finance Comm. Action 6/28/04 FY 05	OFA Revised Estimate 11/12/04 FY 05	OFA Revised Estimate 1/28/05 FY 05		OFA Current Services Estimate 1/28/05 FY 06	OFA Current Services Estimate 1/28/05 FY 07
Revenues	-	ı	13,226.3	13,310.0	13,552.0	13,681.0	I	13,657.0	14,268.0
Expenditures	-	i	13,226.0	13,226.3	13,301.0	13,311.8	i	14,329.6	15,127.6
Balance	300.0	ļ	0.3	83.7	251.0	369.2	I	(672.6)	(859.6)
Maximum Allowable in Budget Reserve (Rainy Day) Fund Potential BRF Deposit Extent to Which BRF Not Fully Funded Spending Cap Comparisons (All Funds): Amount Total Appropriations (Under) Over Cap Amount Over Cap if: Appropriate to the Allowable Cap Level in FY 0 Reduce FY 07 Base to FY 06 New Amount Allo				(129.1)		1,433.0 <u>669.2</u> 763.8	(hypo	650.0 515.8	893.7 754.6
Reasons for FY 06 & FY 07 Shortfalls:							į		[
FY 06 - Unavailable One-Time Revenues & Tax Changes in the General Fund							į	508.4	! ! !
General Fund Growth Rates: Revenue Expenditures						5.3% 6.1%	1	4.0% 6.9%	4.2% 5.6%

Summary of Changes to November 12, 2004 General Fund Surplus/Deficit Projections as of January 28, 2005 (figures in millions)

			FY 05			FY 06			FY 07
Projected Surplus/(Deficit) as of 11/12/04				\$ 251.0	\$	(603.8)		\$	(701.4)
Expenditure Increases Increased deficiency requirements Miscellaneous expenditure increase Total - Expenditure Increases	\$	(18.6) (1.0)	\$ (19.6)						
Expenditure Decreases Increase in projected lapse savings			8.8						
Net Expenditure Increase				(10.8)		(151.8)	[1]		(184.2) [1]
Revenue Increases Corporation Business Tax Personal Income Tax Real Estate Conveyance Tax Federal Grants Miscellaneous Revenue Increases Total - Revenue Increases	\$	79.1 40.0 37.0 25.5 0.1	\$ 181.7						
Revenue Decreases Sales and Use Tax Miscellaneous Revenue Decreases Total - Revenue Decreases	_	(39.8) (12.9)	(52.7)						
Net Revenue Increase				 129.0	_	83.0	[2]	_	26.0 [2]
Projected Surplus/(Deficit) as of 1/28/05				\$ 369.2	\$	(672.6)		\$	(859.6)

^[1] FY 06 and FY 07 expenditures are higher than our November 12, 2004 projections largely because subsequently received actuarial valuations for the state employee and teachers' retirement systems indicated the need for additional funding of \$158.5 million in FY 06 and \$166.8 million in FY 07.

^[2] FY 06 and FY 07 revenues are higher than our November 12, 2004 projections due to miscellaneous revenue adjustments.

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General Fund and Transportation Fund Budget Projections

(as of January 28, 2005)

I. FY 05 General Fund

Our projections for the fiscal year ending June 30, 2005 indicate a potential surplus of \$369.2 million (which represents 2.8% of the budget). This surplus assumes that in addition to the originally budgeted surplus of \$83.7 million, estimated revenues will be \$371 higher than budgeted and estimated expenditures will be \$85.5 million higher than net appropriations. While the projected General Fund surplus is \$369.2 million, this estimate may change if: 1) the level of currently estimated deficiencies grows; 2) if any arbitration awards or collective bargaining agreements are submitted and approved by the legislature or become effective in the absence of legislative rejection; or 3) if revenues are adversely affected by any deterioration in economic conditions.

Revenues

The \$371.0 million net increase in estimated FY 05 General Fund revenue collections is due to increases of \$469.9 million in 6 areas and decreases of \$98.9 million in 3 areas. The revenue increases are: (1) a \$229.0 million increase in the Personal Income Tax; (2) a \$88.3 million increase in the Corporation Tax; (3) a \$49.2 million increase in the Real Estate Conveyance Tax; (4) a \$39.9 million increase in the Oil Companies Tax; (5) a \$38.0 million increase in Rentals, Fines, and Escheats revenue; and (6) a \$25.5 million increase in Federal Grant revenue. The revenue decreases are: (1) a \$50.3 million decrease in the Sales and Use Tax; (2) a \$40.0 million decrease in Transfer to the Resources of the General Fund; and (3) \$8.6 million in modifications to various General Fund revenue sources.

The \$469.9 increase in estimated revenue collections is due to the following:

- (1) The \$229.0 million increase in the **Personal Income Tax** estimate is due to:
 - a) *Estimated Payments:* Anticipated collections from estimated payments have been increased by \$133 million. Revenue collections from third quarter payments (due September 15th) grew by approximately 22% and fourth quarter payments (due January 15th) grew by approximately 30%. Collections through January have exceeded original estimates by about \$82 million. This continued the trend in strong collections observed in first and second quarter payments (due in April and June respectively.) Based on this pattern, the revised FY 05 forecast assumes a growth rate of 17.5% compared to 6.8% assumed in the Finance Committee revenue estimates. Total collections for FY 05 are now forecasted to be \$152.0 million greater than what was originally anticipated at the time the Finance, Revenue, and Bonding Committee adopted revised FY 05 estimates in June 2004.

- b) Final Payments: The revenue from final payments, due April 2005, is anticipated to be \$60 million greater than projected. An examination of historical collections indicates that estimated payments equal about 60% of total non-wage payments and final payments make up the remaining 40%. Therefore, since estimated payments are anticipated to be higher than the initial forecast, final payments have been increased to maintain the historic relationship.
- c) Withholding Payments & Audits: Year-to-date collections from these sources are modestly healthier than initially anticipated, which resulted in a \$17 million increase in the estimate.
- (2) The **Corporation Tax** estimate increased by \$88.3 million because collections are tracking above our targets by about \$76 million. Recent corporate profit reports have been particularly strong in many sectors of the economy including: energy, financial services, home building, information technology, and natural resources. Corporate earnings have been bolstered by improvements in US economic fundamentals, strong foreign economic conditions, especially in China, and strong exports, which have been aided by a weak US dollar.
- (3) **Real Estate Conveyance Tax** collections are anticipated to be \$49.2 million greater than projected. The FY 05 original budget estimate assumed that collections would decline by 10.5% compared to last year. The estimate assumed the state's real estate market would slow down after an extremely robust FY 04 (revenues grew by 35% compared to FY 03) as the demand by buyers diminished and interest rates started to increase. However, collections for the first 5 months of the fiscal year grew by 17%, a gain of \$12.5 million over last year's collections. Since year-to-date collections have exceeded our original estimates by \$26 million we have updated our forecast to reflect current market conditions.
- (4) **Oil Companies Tax** collections are expected to be \$39.9 million higher than anticipated. Year-to-date collections are up by approximately 35% (\$12 million) due to a 70% increase in crude oil prices since the beginning of 2004. The factors that contributed to the increase in crude oil prices are expected to remain influential for the remainder of the fiscal year. These include: (1) very strong demand in Asia, (2) continued concerns in Iraq and the Middle East, and (3) lingering supply concerns in Russia (Yukos), Nigeria, and Norway. Based on this information, the growth rate for the tax was increased to 26% compared to -4.5% assumed in the Finance Committee estimates.
- (5) The \$35.5 million increase in the estimate for **Rentals**, **Fines**, **and Escheats** revenue is due to higher than anticipated proceeds from the sale of unclaimed public securities in the custody of the Office of the State Treasurer. The budget act assumed that \$50 million would be generated from the liquidation of these securities, while the sale actually realized approximately \$88 million.
- (6) The \$25.5 million increase in **Federal Grants** revenue is primarily due to higher expenditures in human services programs that are matched by the federal government and higher Medicaid revenue for prior year claims.

The \$98.9 million decrease in estimated revenue collections is from the following:

- (1) The **Sales and Use Tax** estimate decreased by \$50.3 million because the original projection assumed that collections would grow by 5.1% but year-to-date collections have grown by 3.9%. (The revised estimate reflects a growth rate of 4.0%.) The decrease in Sales Tax collections could be the result of a decline in consumer confidence between August and November, which may have caused some consumers to postpone or delay purchases.
- (2) The amount of revenue **Transferred to the Resources of the General Fund** is anticipated to be \$40 million lower than projected. The FY 05 revenue estimates adopted by the Finance Committee included \$40 million from the sale of bonds securitizing future unclaimed property revenue. However, the revised estimates assume that the bond sale will not occur because OFA's most recent projections for the General Fund indicate that it will end the fiscal year with a surplus greater than \$40 million.
- (3) An additional \$8.6 million in decreases is due to modifications to various General Fund revenue sources that are relatively minor and can be explained by adjustments that were made based on: (a) actual FY 04 collections rolled forward into FY 05, and (b) year-to-date collections for FY 05.

Expenditures

Deficiencies

The \$85.5 million increase in expenditures is largely attributable to projected deficiencies totaling \$80 million. Of this amount, \$53.5 million in net deficiencies are occurring within the Department of Correction (\$23.3 million), Department of Children and Families (\$12 million), the, the Office of Policy and Management – Energy Contingency (\$10 million), the Department of Social Services (\$8 million), the Department of Mental Retardation (\$7.6 million), Department of Public Safety (\$6.5 million) and the Department of Mental Health and Addiction Services (\$5.2 million). Please see the explanations for all FY 05 projected deficiencies which begin on page 8.

Also, projected payments for two non-budgeted accounts are factored in: Adjudicated Claims of \$9 million and Refunds of Escheated Property at \$14 million.

Budgeted Lapses

Lapses anticipated in the budget total \$109.9 million and given the amount of unallocated lapse already identified, our surplus projection assumes that these savings will be achieved and perhaps exceeded by \$17.5 million. The \$109.9 million budgeted savings includes: \$78.6 million in unallocated budgeted lapses; \$25 million in Personal Services (PS) and Other Expenses (OE) holdbacks; \$2.5 million in fleet reductions; and \$5 million from a spend management lapse. The Office of Policy and Management has reduced agency allotments to reflect the imposition of PS and OE holdbacks and the spend management lapse and has indicated that the fleet reduction savings will not be realized.

Major Unallocated Lapses

So far, we have identified \$70 million of the \$78.6 million unallocated lapse anticipated in the budget. Three accounts comprise \$63.9 million of the \$70 million in identified lapses, the reasons for which are described below. Given that nearly all of unallocated lapse has been identified, we have increased our FY 05 unallocated lapse projection by \$20 million.

Unallocated Lapses (figures in \$ millions)

Debt Service	46.5
Miscellaneous Accounts – Fringe Benefits	15.0
Workers' Compensation	<u>2.4</u>
Total – Significant Identified Lapsing Appropriations	63.9
Other Identified Lapses (less than \$1 million each)	6.1
Unidentified Lapses	8.6
Increase in Projected Lapse Given Amount Already Identified	<u>20.0</u>
Total – Projected Unallocated Lapses	98.6

Debt Service - A \$46.5 million anticipated lapse in Debt Service is the largest significant lapse identified at this time. This figure represents 3.5% of its FY 05 appropriation of \$1,311.2 million and is a combination of \$46.6 million in savings and \$0.1 million in increased expenditures. The projected savings are: (1) \$25.7 million in savings due to changes in the issuance schedule and lower than anticipated interest rates, (2) \$18 million in premiums received on General Obligation (GO) bonds issued in May 2004 and December 2004, (3) \$0.2 million in savings from a October 2004 refunding of tax incremental financing (TIF) bonds, (4) \$2.3 million in savings from arbitrage rebate payments, rebate fees and trustee fees, and (5) \$0.4 million in savings from a variety of other sources. (Note that bond purchasers pay a premium to receive a higher interest rate than the one at which the bonds would otherwise have sold.)

The increase of \$0.1 million is due to the addition of a line item for fees paid to the bank trustees that oversee bonds issued for the UConn 2000 infrastructure program. (The fees were previously paid out of lapsed debt service funds at the end of the fiscal year.)

Miscellaneous Accounts - Fringe Benefits - The fringe benefit accounts have a net lapse of \$15.0 million. This is approximately 1% of the total appropriation of \$1.3 billion for all ten accounts. Two accounts, unemployment compensation and state employees health service costs have lapses of \$1 million and \$15 million, respectively. The state employee health service cost account lapse, which is

approximately 4% of the accounts' appropriation, is largely the result of new hires choosing lower cost health plans. The total lapse of \$16 million is offset by a deficiency of \$1 million in employer social security.

Workers' Compensation - The Department of Administrative Services workers' compensation claims account is projected to have a lapse of approximately \$2.4 million, which represents 12.4% of its FY 05 appropriation of \$19.5 million.

The lapse is the result of several factors: a stabilization in claim expenditures during the first six months of FY 05; new loss-control measures; and no lump sum full and final settlement payments. This account is responsible for the workers' compensation costs for 84 state agencies.

• State Employee Wage Increases

A range of \$5.5 million to \$21.4 million may need to be added to the FY 05 budget depending upon whether a 1 year wage freeze is extended or not to 6 contracts which have expired as of 6/30/03 and 6/30/04 and remain unsettled. Please refer to the "Watch List" of Potential Additional FY 05 Deficiencies on page 21 for additional information.

Budget Reserve (Rainy Day) Fund Status

It is anticipated that the State Comptroller will close the books on FY 04 by February 28, 2005 and that the FY 04 surplus could approach \$300 million. The amount of surplus realized would be deposited in the Budget Reserve (Rainy Day) Fund which currently contains a zero balance. The maximum allowable in the Budget Reserve Fund is 10% of the amount of the net General Fund appropriations for the fiscal year in progress. With net General Fund appropriations for FY 05 totaling \$13,226.3 million, the maximum allowable in the Budget Reserve Fund is \$1,322.6 million or \$1,022.6 more than potentially deposited assuming that a full \$300 in FY 04 surplus is realized.

The \$594.7 million balance that remained in the Budget Reserve Fund in FY 01 was used to partially cover the \$817.1 million deficit in FY 02. The remaining FY 02 deficit balance of \$222.4 million was carried forward into FY 03 and financed with the issuance of Economic Recovery Notes during the fiscal year. It should be noted that PA 03-2 (the deficit mitigation act) increased the maximum allowable in the Budget Reserve Fund from 7.5% to 10% of the amount of the net General Fund appropriations for the fiscal year in progress. PA 02-118 had previously increased the maximum from 5% to 7.5%.

PA 03-1 (September 8 Special Session) authorized the State Treasurer to issue 5-year, tax exempt, general obligation "Economic Recovery Notes" to finance the \$96.6 million General Fund deficit in FY 03. The act provided that no principal would be paid during the fiscal year of issuance.

FY 05 General Fund Summary as of January 28, 2005 (in millions)

	Budget <u>Plan [1]</u>	Increases (Decreases)	<u>Projected</u>
Revenues			
Taxes	\$ 9,441.1	\$ 369.2	\$ 9,810.3
Other Revenue	1,151.5	21.0	1,172.5
Other Sources [2]	<u>2,717.4</u>	(19.2)	2,698.2
Total Revenue	\$ 13,310.0	\$ 371.0	\$ 13,681.0
Appropriations			
Original Appropriations - Gross	\$ 13,336.2	\$ -	\$ 13,336.2
Plus:			
Deficiency Requirements	-	80.0	80.0
Adjudicated Claims	-	9.0	9.0
Refunds of Escheated Property	-	14.0	14.0
Less:			
Lapses [3]	<u>(109.9)</u>	<u>(17.5)</u>	<u>(127.4)</u>
Total Expenditures [4]	\$ 13,226.3	\$ 85.5	\$ 13,311.8
Surplus/(Deficit) from Operations for FY 05 [5]	\$ 83.7	\$ 285.5	\$ 369.2

^[1] The budget plan revenues for FY 05 are the estimates of the Finance, Revenue and Bonding Committee and were initially adopted on April 29, 2004, but were subsequently revised for FY 05 per Section 2-35 (CGS) by the committee on June 28, 2004.

[3] The breakdown for budgeted lapses is as follows:

unallocated budgeted lapses	\$ (78.6)	\$ (20.0)	\$ (98.6)
general PS and OE reductions (holdbacks)	(25.0)	-	(25.0)
Fleet Reduction	(2.5)	2.5	-
Spend Management Lapse	(3.8)		(3.8)
Total - Lapses Originally Budgeted	\$ (109.9)	\$ (17.5)	\$ (127.4)

^[4] Excludes expenditures from prior year carryforwards and appropriations from projected surplus.

Of the 17 contracts that have not agreed to a wage freeze in any one year, 6 have contract termination dates which could potentially require funding during the current biennium. FY 05 costs could range from \$5.5 million to \$21.4 million depending upon whether a 1 year wage freeze is extended or not to these 6 expired contracts. The remaining 11 contracts would not likely require funding until the next biennium (FY 06 and FY 07).

The extent to which agency budgets and the Reserve for Salary Adjustments account can absorb any of the increases which may occur during the current biennium is uncertain at this time. Some level of additional appropriation may be likely and will ultimately depend as well upon the number of unsettled contracts or arbitration awards submitted for approval prior the end of the current fiscal year and whether any include wage concessions similar to those contained within agreements already approved.

Note: It is anticipated that the State Comptroller will close the books on FY 04 by February 28, 2005 and that the FY 04 surplus could approach \$300 million. The amount of surplus realized would be deposited in the Budget Reserve (Rainy Day) Fund which currently contains a zero balance. The maximum allowable in the Budget Reserve Fund is 10% of the amount of the net General Fund appropriations for the fiscal year in progress. With net General Fund appropriations for FY 05 totaling \$13,226.3 million, the maximum allowable in the Budget Reserve Fund is \$1,322.6 million or \$1,022.6 more than potentially deposited assuming that a full \$300 million in FY 04 surplus is realized.

^[2] The budget plan's revenue from Other Sources includes \$40 million of one-time revenue to securitize unclaimed property per the budget act which now appears unnecessary given that the State Treasurer has liquidated \$38 million more than the originally anticipated \$50 million from unclaimed securities alone and a surplus is projected for FY 05.

^[5] The projected surplus for FY 05 could be lower if any additional arbitration awards or collective bargaining agreements (for which funding has not been specifically provided in the budget) are approved by the legislature or become effective in the absence of legislative rejection. Of the 33 contracts, 16 (covering slightly more than half of state employees) are settled/funded and have agreed to a one year wage freeze and 17 have not yet agreed to a wage freeze in any one year.

FY 05 General Fund Revenue Estimates as of January 28, 2005 (in thousands)

	Budget Plan		OFA	OFA E	A Estimates	
_	Growth	FY 05	Over(Under)	Growth	FY 05	
	Rate {1}	Estimate	Plan	Rate {1}	Estimate	
Taxes						
Personal Income	5.2	\$5,131,000	\$229,000	8.5	\$5,360,000	
Sales and Use	5.1	3,320,300	(50,300)	3.9	3,270,000	
Corporations	8.0	501,700	88,300	23.6	590,000	
Public Service Corporations	-	189,400	7,600	4.0	197,000	
Inheritance and Estate	3.0	166,100	-	3.0	166,100	
Insurance Companies	3.0	234,800	5,200	3.0	240,000	
Cigarettes	(1.5)	266,000	-	(4.3)	266,000	
Real Estate Conveyance	(10.5)	145,800	49,200	10.3	195,000	
Oil Companies	(4.5)	89,600	39,900	26.0	129,500	
Alcoholic Beverages	-	43,500	200	-	43,700	
Admissions, Dues and Cabaret	2.0	33,100	100	2.0	33,200	
Miscellaneous	(5.7)	33,800	<u>=</u>	(5.7)	33,800	
Total Taxes		10,155,100	369,200		10,524,300	
Refunds of Taxes		(700,000)	-		(700,000)	
R & D Credit Exchange	_	(14,000)	<u>-</u>	_	(14,000)	
Taxes Less Refunds	_	9,441,100	369,200	_	9,810,300	
Other Revenue						
Transfer Special Revenue		283,100	(7,100)		276,000	
Indian Gaming Payments		430,000	(10,000)		420,000	
Licenses, Permits and Fees		138,100	-		138,100	
Sales of Commodities and Services		36,000	-		36,000	
Rentals, Fines and Escheats		144,500	35,500		180,000	
Investment Income		15,300	(3,300)		12,000	
Miscellaneous		105,000	5,900		110,900	
Refunds of Payments	_	(500)	<u>-</u>	_	(500)	
Total Other Revenue		1,151,500	21,000		1,172,500	
Other Sources					-	
Federal Grants		2,469,600	25,500		2,495,100	
Transfer to the Resources of the General Fund		219,800	(40,000)		179,800	
Transfer from Tobacco Settlement Fund		113,000	(4,700)		108,300	
Transfer to Other Funds		(85,000)			(85,000)	
Total Other Sources		2,717,400	(19,200)	-	2,698,200	
Total Revenue		<u>\$13,310,000</u>	<u>\$371,000</u>		<u>\$13,681,000</u>	

^{1} Tax growth rates reflect adjustments for rate and base changes.

Projected FY 05 General Fund Deficiencies as of January 28, 2005

Note: The projected OPM deficiencies indicated in the first block of each table below were reported on January 20, 2005.

Ethics Commission

			OFA
OPM	OFA	Less:	Remaining
Net Deficiency	Net Deficiency	Available Funds	Deficiency
\$(36,000)	\$(22,000)	\$2,791	\$(19,209)

The Ethics Commission has a projected net deficiency of \$22,000, which represents 2.5% of its FY 05 appropriation of \$871,078. This assumes that a Spend Management holdback of \$2,791 is not released. If the holdback is released, an estimated remaining deficiency of \$19,209 would result.

The \$22,000 net deficiency results from a shortfall in the Lobbyist Electronic Filing System account. The lobbyist registration, reporting, and the statement of financial interest disclosure modules need to be upgraded which will require a contractual agreement with the Department of Information Technology (DOIT). The funds are needed to pay DOIT for hosting, database support, application maintenance for troubleshooting, and development costs for these online applications. The \$22,000 deficiency results from this upgrade. The potential for funding to support additional staffing has been postponed by the Governor pending possible reorganization of the agency.

Office of Policy and Management – Energy Contingency

			OFA
OPM	OFA	Less:	Remaining
Net Deficiency	Net Deficiency	Available Funds	Deficiency
\$(10,000,000)	\$(10,000,000)	\$0	\$(10,000,000)

The Office of Policy Management has a projected net deficiency of \$10 million in an Energy Contingency account which was not budgeted in FY 05. In FY 04 General Fund expenditures for all energy costs (electricity, natural gas, motor vehicle and fuel oil) was \$50.9 million. The FY 05 appropriation for agency energy costs does not include an inflationary increase, thus any additional requirements will result in a deficiency between \$4.1 million and \$11.2 million, as oil and natural gas prices have risen significantly. The actual level of deficiency is contingent on the rate of increase of these costs, particularly among natural gas and district heating, which is anticipated to increase between 6% and 38%.

Department of Veterans' Affairs

			OFA
OPM	OFA	Less:	Remaining
Net Deficiency	Net Deficiency	Available Funds	Lapse
\$(0)	\$(373,500)	\$456,754	\$83,254

The Department of Veterans' Affairs has a projected net deficiency of \$373,500, which represents 1.3% of its General Fund FY 05 appropriation of \$27.9 million. This assumes that a Personal Services holdback of \$178,293, an Other Expenses holdback of \$181,429 and a Spend Management holdback of \$97,032 are not released, however, \$550,000 in Personal Services is made available via FAC transfer. If the holdbacks are released, an estimated surplus of \$83,254 would result.

The deficiency is attributed to the Other Expenses account due to various operating costs and expenditures benefiting veterans at the department's facilities. Various Other Expenses (OE) costs such as food & beverage (with increased number of veterans receiving daily meals); temporary nursing services being provided in the healthcare facility (resulting from a delay in filling full-time nurse positions); and increased medical supplies. Two other factors that may reduce the shortfall are: 1) The level of Personal Services account funding that will be available to transfer to OE (through a future FAC action as mentioned above). Personal Services funding is available due to delay in filling permanent nurse positions; and 2) Available funding in the Institutional General Welfare Fund (IGWF). The IGWF operates under the provisions in statute and is available for use by the department with funds received from patient billing and estate collections. IGWF funds are used to pay for costs benefiting veterans at the facility, similar to the OE account.

Department of Public Works

			OFA
OPM	OFA	Less:	Remaining
Net Deficiency	Net Deficiency	Available Funds	Deficiency
\$(1,500,000)	\$(2,500,000)	\$606,781	\$(1,893,219)

The Department of Public Works has a projected net deficiency of \$2.5 million, which represents 6% of its FY 05 appropriation of \$41.6 million. This assumes that a Personal Services holdback of \$50,046, an Other Expenses holdback of \$529,589 and a Spend Management holdback of \$27,146 are not released. If the holdbacks are released, an estimated remaining deficiency of \$1,893,219 million would result.

The \$2.5 million net deficiency, which is in the Management Services account, results from the carry forward of \$1.29 million in unpaid expenses from FY 04 and a projected FY 05 shortfall of \$1 million for repairs and maintenance to buildings under the agency's care and control and \$0.21 million for security services. The FY 04 carry forward is composed of \$0.2 million for repairs and maintenance, \$0.23 million for security services, \$0.2 million for snow removal services, and \$0.66 million in bills for services rendered in June 2004.

Department of Public Safety

			OFA
OPM	OFA	Less:	Remaining
Net Deficiency	Net Deficiency	Available Funds	Deficiency
\$(6,450,000)	\$(6,450,000)	\$2,269,579	\$(4,180,421)

The Department of Public Safety has a projected net deficiency of \$6.45 million, which represents 4.9% of its FY 05 appropriation of \$130.7 million. This assumes that a Personal Services holdback of \$850,810, an Other Expenses holdback of \$574,495 and a Spend Management holdback of \$844,274 are not released. If the holdbacks are released, an estimated remaining deficiency of \$4.2 million would result.

The \$6.45 million net deficiency occurs in two areas: Personal Services (\$3.575 million) and Other Expenses (\$2.875).

The shortfall in Personal Services results from a partial inability to meet a \$4 million reduction that was included in the revised FY 05 budget. This reduction related to collections for reimbursements for troopers assigned to certain facilities (such as Bradley Airport). In past years, the agency, for budgeting purposes, was allowed to retain about \$6 million of the \$12 million collected for trooper reimbursements. As part of the Revised FY 05 Budget, the agency's retention of these reimbursements was reduced by \$4.0 million while total reimbursements received dropped by \$2.0 million for an effective budgetary loss of \$6 million.

The agency could have absorbed these reductions but was given the approval to conduct a trooper training class of 70 (the agency lost 57 troopers due to early retirement) and to refill 40 civilian positions (the agency lost 59 civilian positions due to layoff). The cost of these refills is about \$3.4 million.

In addition being unable to meet the \$4 million reduction, the shortfall in Personal Services results from an estimated additional fifteen positions for the newly created Department of Emergency Management and Homeland Security. The cost of the new positions is currently estimated at \$225,000.

The shortfall in Other Expenses relates to a range of higher than expected cost areas and the carry forward of FY 04 bills into FY 05 including: motor vehicle fuel (including a 20% per gallon cost increase over last year), motor vehicle maintenance, IT hardware and data contract costs, electricity, and oil/natural gas/propane and aircraft fuel costs.

In addition to these items, the replacement of body armor was not sufficiently budgeted. The body armor issued to all Troopers must be replaced every five years. Due to a disproportionate number being issued in FY 99 and a new training class estimated to graduate 56 Troopers, 585 need to be purchased. The average number of replacements over the last two years was 149. The cost of the body armor is estimated to be up to \$325,000.

Office of Child Advocate

			OFA
OPM	OFA	Less:	Remaining
Net Deficiency	Net Deficiency	Available Funds	Deficiency
\$(70,000)	\$(70,000)	\$2,265	\$(67,735)

The Office of Child Advocate has a projected net deficiency of \$70,000, which represents 11.4% of its FY 05 appropriation of \$612,470. This assumes that a Spend Management holdback of \$2,265 is not released. If the holdback is released, an estimated remaining deficiency of \$67,735 would result.

The \$70,000 net deficiency results from 4 contracts with 2 vendors that were unanticipated prior to FY 05. These contracts were entered into to provide technical assistance and consultation with the agency's caseload since the agency no longer has a staff attorney.

Department of Public Health

			OFA
OPM	OFA	Less:	Remaining
Net Deficiency	Net Deficiency	Available Funds	Deficiency
\$(1,753,500)	\$(1,736,528)	\$419,564	\$(1,316,964)

The Department of Public Health has a projected net deficiency of \$1.7 million, which represents 2.5% of its FY 05 appropriation of \$69.1 million. This assumes that a Personal Services holdback of \$216,775, an Other Expenses holdback of \$153,671 and a Spend Management holdback of \$49,118 are not released, but that \$25,000 in lapsing funds under various accounts is made available via FAC transfer. If the holdbacks are released, an estimated remaining deficiency of \$1.3 million would result.

A \$1.58 million deficiency is attributable to bills incurred in FY 04 being paid in the current fiscal year due to delays in processing payments through the CORE-CT accounting system. An equivalent amount lapsed under these same accounts on June 30, 2004.

An additional \$0.15 million shortfall is expected under the Local and District Departments of Health account. This grant supports per capita subsidy payments to health districts, full time health departments, and part time health departments. The deficiency is attributable to (a) an unanticipated population increase, (b) the formation of a new health district, (c) the merger of a full time health department into an adjacent health district, and (d) the conversion of two town health departments from part time to full time health status. Statutorily authorized per capita subsidies for health districts exceed those for full time health departments. Part time health departments are eligible for the lowest per capita subsidy.

Department of Mental Retardation

			OFA
OPM	OFA	Less:	Remaining
Net Deficiency	Net Deficiency	Available Funds	Deficiency
\$(7,400,000)	\$(7,600,000)	\$3,145,545	\$(4,454,455)

The Department of Mental Retardation has a projected net deficiency of \$7.6 million, which represents 1% of its FY 05 appropriation of \$741.8 million. This assumes that a Personal Services holdback of \$2,224,536, an Other Expenses holdback of \$624,896 and a Spend Management holdback of \$296,113 are not released. If the holdbacks are released, an estimated remaining deficiency of \$4.45 million would result. The deficiency is the result of a projected shortfall in four accounts: Other Expenses (\$1.2 million), Workers' Compensation (\$1.2 million), Employment Opportunities and Day Services (\$1.48 million) and the Community Residential Services (\$3.7 million).

Other Expenses and Workers' Compensation - The Other Expenses shortfall of \$1.2 million is due to various clients and operational costs. The FY 05 Other Expenses estimated expenditures is \$22.8 million, a 2.5% increase from FY 04 expenditures. As a result of the Workers' Compensation shortfall (\$1.2 million), the FY 05 estimated expenditures for this account reflect a 1.6% reduction from FY 04 expenditures.

Employment Opportunities and Day Services - The \$1.48 million deficiency is the result of increased demand on day programs by the number of Ageouts and High School graduates. The ageouts include individuals that will be aging out of existing services with the Department of Children and Families or the local educational authorities (LEA's). The high school graduates include individuals who are living at home with their families and will be graduating from the school systems and in need of a day program. Due to the level of funding provided in the FY 05 budget and the increased number of ageouts and high school graduates, a net deficiency of \$1.48 million is projected. There are a total of 76 additional day programs (33 ageouts and 43 high school grads) than originally projected. It is anticipated that \$1.3 million of the federal SSBG (Social Services Block Grant) carry forward funding will be utilized along with the \$1.48 million deficiency funding to fully support these day programs.

Community Residential Services - A \$3.7 million shortfall is anticipated in the Community Residential Services account due to two factors: 1) \$1.8 million in residential services for ageouts due to the level of funding provided in the FY 05 budget and the increased number of ageouts (15 additional residential placements); and 2) \$1.9 million for unmet residential needs due to the FY 04 conversions of publicly operated Community Living Arrangements (CLA's, otherwise known as group homes) to private contracts. The FY 04 Conversion project was started during FY 04 due to the changes in staffing from the ERIP (early retirement incentive plan) and regional consolidation. The total contracted amount in FY 05 in the community residential account as a result of the FY 04 conversions is \$10.8 million, of which \$4.7 million is anticipated to be funded from a future FAC action during this fiscal year (transfer from the Personal Services account to the Community Residential account). Further, the department anticipates that in order to meet the total contractual amount, a \$1.9 million shortfall in this account will result. This assumes that existing FY 05 dollars, of

approximately \$4.2 million, are utilized in this account to fund part of the conversion contracts. It is anticipated that the delay of the new FY 05 conversions will allow for the use of \$2.2. million with the remaining \$1.96 million (of the \$4.2 million) utilized from other existing funding previously not budgeted for this purpose. Reflected in the table below is the funding applied to the \$10.8 million conversion contracts.

FY 04 Conversions - Contracts for FY 05 (in million	ons)
FY 05 Total Value of Contracts	\$10.8
Apply Future FAC from PS	(\$4.7)
Apply existing \$ within residential account	(\$4.2)
Balance Deficiency Request	(\$1.9)

It should be noted that the FY 05 Midterm Budget Adjustments did not include any new dollars or transfers among accounts to implement the FY 04 Conversions (only a transfer to DSS for room & board costs). It was anticipated that a future FAC action during FY 05 would fully cover the costs of the FY 04 conversion contracts.

Department of Mental Health and Addiction Services

			OFA
OPM	OFA	Less:	Remaining
Net Deficiency	Net Deficiency	Available Funds	Deficiency
\$(6,700,000)	\$(5,225,000)	\$2,427,748	\$(2,797,252)

The Department of Mental Health and Addiction Services has a projected net deficiency of \$5.2 million, which represents 1.2% of its FY 05 appropriation of \$449.1 million. This assumes that a Personal Services holdback of \$1,241,713, an Other Expenses holdback of \$709,441 and a Spend Management holdback of \$476,594 are not released. If the holdbacks were released, an estimated remaining lapse of \$2.8 million would result.

The \$5.2 million net deficiency is primarily due to expenditures in the Other Expenses, Behavioral Health Medications, and Professional Services accounts. Other Expenses has a projected deficiency due mainly to increased repair, utility and maintenance costs at Connecticut Valley and Cedarcrest Hospitals. A \$1.5 million deficiency is projected in the Behavioral Health Medications account due to continued increases in drug costs. A \$2.3 million deficiency is projected in the Professional Services account due to the utilization of temporary agency nurses at Connecticut Valley Hospital. This expenditure is necessary due to a general shortage of nurses in the state that has led to difficulties in filling permanent nursing positions. These deficiencies are partially offset by projected surpluses in the Personal Services, Special Populations, and Adult Medicaid Rehabilitation Option accounts.

Department of Social Services

			OFA
OPM	OFA	Less:	Remaining
Net Deficiency	Net Deficiency	Available Funds	Deficiency
\$(4,400,000)	\$(7,950,000)	\$3,427,660	\$(4,522,340)

The Department of Social Services has a projected net deficiency of \$7.95 million, which represents 0.1% of its FY 05 appropriation of \$3,916.6 million. This assumes that a Personal Services holdback of \$749,857, an Other Expenses holdback of \$2,489,609 and a Spend Management holdback of \$188,194 are not released. If the holdbacks are released, an estimated remaining deficiency of \$4.5 million would result.

The \$7.95 million net deficiency is primarily due to expenditures in the Medicaid, ConnPACE, Connecticut Home Care and Supplemental Assistance programs. These shortfalls are offset by potential lapses in the Temporary Family Assistance and Child Care Subsidies accounts.

Medicaid – The Medicaid program has a projected deficiency of \$9.7 million (.3% of the original appropriation). This deficiency is the result of slightly higher than anticipated medical costs for the first six months of the fiscal year.

ConnPACE - A deficiency of approximately \$1.5 million is projected for the Connecticut Pharmaceutical Assistance Contract to the Elderly and the Disabled (ConnPACE) program. This shortfall is primarily attributable to fewer than projected enrollees obtaining Medicare Prescription Drug Discount Card (DDC) Transitional Assistance benefits and delays in integrating ConnPACE with the new federal program.

Savings of \$16.9 million were included within PA 04-216 (the budget bill) to reflect reduced program costs due to making participation in the new DDC program a condition of continued ConnPACE eligibility for those enrollees who (a) are Medicare eligible, and (b) are eligible for new federal Transitional Assistance drug benefits – i.e., those with incomes at or below 135 percent of the federal poverty level. This savings estimate assumed that a portion of the prescription costs of an estimated 21,700 individuals would be shifted from the state to the federal government as of July 1, 2004. Revised estimates project that approximately 16,300 enrollees will be eligible for DDC Transitional Assistance benefits. Additionally, delays were experienced in the course of enrolling clients with the thirteen Drug Discount Card vendors selected by the state.

Connecticut Home Care Program - The Connecticut Home Care Program has a projected deficiency of \$3.2 million (9% of the original appropriation). This deficiency is due to continued caseload growth as well as increased medical costs. Although not legally an entitlement, the state has treated the home care program as such, with a no waiting list enrollment policy. This has led to significant program growth in recent years.

Supplemental Assistance - Two programs within Supplemental Assistance have projected deficiencies. The Aid to the Disabled program has a projected deficiency of \$2 million while the Old Age Assistance program has a projected deficiency of \$600,000. These deficiencies (4% of the original appropriations) are due to higher than anticipated cost-per-case over the first six months of FY 05.

Department of Education

			OFA
OPM	OFA	Less:	Remaining
Net Deficiency	Net Deficiency	Available Funds	Deficiency
\$(1,900,000)	\$(1,900,000)	\$1,545,219	\$(354,781)

The Department of Education has a projected net deficiency of \$1.9 million, which represents approximately 0.1% of its FY 05 appropriation of \$2,095.9 million. This assumes that a Personal Services holdback of \$981,755, an Other Expenses holdback of \$389,102 and a Spend Management holdback of \$174,362 are not released. If the holdbacks are released, an estimated remaining deficiency of \$354,781 million would result.

The \$1.9 million net deficiency results from the Sheff v. O'Neill settlement. The Department of Education needs authorization from the legislature to expend further funds for the settlement as the grant account for magnet schools is formula driven and this expenditure goes beyond the formula driven amounts.

Department of Correction

			OFA
OPM	OFA	Less:	Remaining
Net Deficiency	Net Deficiency	Available Funds	Deficiency
\$(23,300,000)	\$(23,300,000)	\$6,438,668	\$(16,861,332)

The Department of Correction is projecting a net deficiency of \$23.3 million, which represents 4.2% of its FY 05 appropriation of \$548.5 million. This assumes that a Personal Services holdback of \$2,851,199, an Other Expenses holdback of \$1,818,782 and a Spend Management holdback of \$1,768,687 are not released. If the holdbacks were released, an estimated remaining deficiency of \$16.9 million would result. The projected deficiency has grown by \$9.8 million since a \$13.5 million deficiency figure reported in November 2004.

The deficiency occurs in four areas as follows:

Personal Services	\$ 20,925,000
Other Expenses	1,000,000
Out of State Beds	75,000
Inmate Medical Services	1,300,000
Total	23,300,000

The Original FY 05 budget included funding for a projected inmate population of over 20,000 inmates. The Revised FY 05 Budget, which reduced agency funding by \$28 million, was based on a leveling of the inmate population along with about \$13.4 million in funding for prison overcrowding initiatives, including residential program funding for 440 beds. The incarcerated population during FY 05 has averaged about 18,650.

Department of Children and Families

			OFA
OPM	OFA	Less:	Remaining
Net Deficiency	Net Deficiency	Available Funds	Deficiency
\$(13,750,000)	\$(12,030,013)	\$3,291,708	\$(8,738,305)

The Department of Children and Families has a projected net deficiency of \$12.0 million, which represents 1.9% of its FY 05 appropriation of \$642.6 million. This assumes that a \$0.3 million lapse in the Board and Care for Children – Adoption account, a \$1.0 million lapse in the Board and Care for Children – Foster account, and a \$0.4 million lapse in the Workers' Compensation Claims account are made available via FAC transfer, but that a Personal Services holdback of \$1,817,441, an Other Expenses holdback of \$1,141,281 and a Spend Management holdback of \$332,986 are not released. If the holdbacks are released, an estimated remaining deficiency of \$9.0 million would result.

Contributing to the \$13.8 million gross deficiency (prior to FAC transfer of \$1.8 million) are shortfalls of:

- \$2.3 million (1% of the original budget) in Personal Services, primarily attributable to unexpected costs associated with supporting 40 durational social workers needed to allow the agency to maintain compliance with caseload standards set forth under an agreement with the federal court. Funding for this purpose was not included within the revised FY 05 budget act.
- \$1.1 million (2.8% of the original budget) in Other Expenses, primarily attributable
 to costs incurred to support the 40 additional positions discussed above, higher
 than anticipated cellular and long distance phone charges and unbudgeted costs
 associated with improvements and alterations to the Connecticut Juvenile
 Training School (CJTS) in Middletown.

The CJTS improvements, at a cost of \$464,550, are one component of an overall facility upgrade intended to improve service delivery to its residents. On October 29, 2004, the Bond Commission approved a request for authorization of \$609,000 to support various capital projects at the facility. These funds will be supplemented by \$155,000 from the Capital Equipment Purchase Fund, bringing the total funding dedicated to upgrading the Training School to \$1,228,550.

Items to be supported with General Fund dollars include:

In bedrooms:	
Provide desk and chair units	\$ 120,050
Provide additional storage units	94,500
Install cork boards	10,000
Install new carpeting	25,000

In other areas:	
Install carpeting in dayrooms of living units	42,000
Establish a reading room on each of nine living units/purchase	
furniture and reading materials	45,000
Install staging system and safety apparatus for creating wall murals	15,000
Outfit unit in now closed high security building (Building 2) to be an	
alternative school	25,000
Create an art studio in Building 2	25,000
Establish a computer lab on each of nine living units	63,000
Total	\$ 464,550

• \$2.3 million (245.6% of the original budget) in the Emergency Needs account, and \$3.1 million (44.1% of the original budget) in the Individualized Family Supports accounts, attributable primarily to payments in excess of budgeted amounts for emergency needs and discretionary/flexible funds.

Per department policy, child protective services workers may request the authorization of discretionary/flexible funds to obtain needed services and/or goods when such services or goods (a) are intended to enhance family preservation and reunification, (b) are individualized, (c) are time limited, and (d) do not supplant existing services to prevent out-of-home placement and facilitate reunification.

An October 7, 2003 stipulated agreement between the parties to the Juan F. Consent Decree required the department "to establish a discretionary funds pool of \$1 million for meeting emergency needs of class members pending DCF's completion of a comprehensive needs assessment using a methodology approved by the (DCF Court) Monitor." The revised FY 05 Appropriations Act included \$950,000 for this same purpose under a newly created Emergency Needs account. An additional \$4.6 million was appropriated under the Individualized Family Supports account to support discretionary/flexible fund payments, bringing the total available for this service type to approximately \$5.6 million.

As of December 2004, actual expenditures under the Emergency Needs account were approximately \$1.6 million, while discretionary/flexible fund expenses under the Individualized Family Supports account were slightly more than \$3.8 million (for a combined total of about \$5.4 million). Combined year-end expenditures of \$11 million are projected.

The DCF Court Monitor's Office recently issued findings regarding these discretionary funds. One hundred (100) of 1,089 payments made from April to September 2004 were sampled. They ranged in value from \$24 to \$4,200 (average of \$556).

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¹ The needs assessment was submitted to the DCF Court Monitor on October 28, 2004.

The number of payments by service type is shown in the following table:

SERVICE/GOOD	# OF PAYMENTS
camp/recreational program	18
security deposit	12
heating/electricity bill	10
undefined	7
clothing	6
rent to avoid eviction	6
counseling	6
beds/furniture	5
daycare	4
therapeutic mentor and education	4
medical or dental need	3
licensing related fees and supervised visitation	3
emergency shelter	2
phone bill/utility	2
one-to-one services	2
food	1
transportation	1
baby room necessities	1
court ordered payment to maternal grandmother	1
drivers license examination	1
employment assistance	1
graduation expense	1
in-home supports	1
prom	1
respite	1
Total	100

- \$0.6 million (17.4% of the original budget) in the Juvenile Justice Outreach Services account, due to unbudgeted costs of \$376,068 for additional outreach and tracking services for male juvenile justice clients and \$200,000 for additional juvenile justice evaluations.
- \$4.3 million (2.9% of the original budget) in the Board and Care for Children –
 Residential account. Of this, \$3.1 million is associated with costs in excess of
 budgeted for services provided in collaboration with the Department of Mental
 Retardation.

Additionally, a \$1.0 million shortfall is attributable to the development of two new group homes. Partial year funding will be provided to Family and Children's Aid, Inc. (Danbury) for a 6-bed group home for children 6 – 12 years of age with serious emotional and psychiatric disturbance who have had lengthy stays at Riverview Hospital (or other psychiatric inpatient units) due to the lack of appropriate treatment and placement options. Additionally, Community Health Resources has been selected to develop a 6-bed group home for adolescent girls 14-18 years of age who are stepping down from DCF-operated residential facilities (Connecticut Children's Place, High Meadows). Funding for these two group homes was not included within PA 04-216. Their annualized cost is

estimated at \$2 million. Also, \$0.8 million in unanticipated costs are associated with the development of five unbudgeted group homes.

These costs are partially offset by approximately \$0.2 million in unobligated funds that were carried forward from FY 04 and \$0.4 million in savings due to a reduction in residential placements and payments.

Public Defender Services Commission

			OFA
OPM	OFA	Less:	Remaining
Net Deficiency	Net Deficiency	Available Funds	Deficiency
\$(875,000)	\$(875,636)	\$269,182	\$(606,454)

The Public Defender Services Commission has a projected net deficiency of \$875,636, which represents 2.6% of its FY 05 appropriation of \$33.9 million. This assumes that a Personal Services holdback of \$216,330, an Other Expenses holdback of \$36,582, and a Spend Management holdback of \$16,270 are not released. If the holdbacks are released, an estimated remaining deficiency of \$606,454 would result.

The \$875,636 net deficiency results from anticipated shortfalls in the non-contractual Special Public Defenders (SPDs) and Expert Witnesses accounts. Greater than expected case assignments and billed hours in the current fiscal year, in addition to \$131,000 in FY 04 obligations carried forward into the current fiscal year, contribute to an estimated, FY 05 gross deficiency of \$694,642 in the non-contractual SPDs account. The projected FY 05 gross deficiency in the agency's Expert Witnesses account is \$180,994, and is related to costs for services of psychiatric and forensic professionals.

Summary of General Fund Lapsing Appropriations and Other Reductions for FY 05 as of January 28, 2005 (figures in millions)

Status of Budgeted Lapses:

Debt Service	\$	46.5		
Miscellaneous Accounts - Fringe Benefits		15.0		
Workers' Compensation	_	2.4		
Total - Significant Identified Lapsing Appropriations	\$	63.9		
Other Identified Lapses (less than \$1 million each)		6.1		
Unidentified Lapses		8.6		
Increase in Projected Lapse Given Amount Already Identified	_	20.0		
Subtotal			\$	98.6
Other Reductions:				
Other Reductions: Personal Services Reduction (holdback)		14.0		
		14.0 11.0		
Personal Services Reduction (holdback)				
Personal Services Reduction (holdback) Other Expenses Reduction (holdback)	_			

Total Frojected Lapses Anticipated in the Budget	Total Projected Lapses Anticipated in the Budget	\$ <i>127.4</i>
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"Watch List" of Potential Additional FY 05 Net Deficiencies as of January 28, 2005

Potential Magnitude of FY 05 Net Deficiency Minimum Maximum

Agency / Account / Description

General Fund:

DPW - The state's lease for the 55 Elm Street building in Hartford, which houses the offices of the State Treasurer, the Comptroller and the Attorney General, expired on November 15, 2004. The Department of Public Works (DPW) has indicated that as part of the negotiation for a new lease with the building owner, the Konover Group, a holdover provision in the old lease will not be invoked until February 15, 2005. The provision stipulates that the state will rent the space on a monthly basis at twice the rate that it paid under the old lease. If it were invoked, the state would pay the increased rate retroactive to December 1, 2004. Since the state paid \$291,666 per month under the expired lease, the state will pay double this amount. In the worst-case scenario the state will have a shortfall of \$2.042 million in FY 05 (i.e., if the state paid an additional \$291,666 per month for 7 months).

It should be noted that in a November 4, 2004 letter to DPW Commissioner James Fleming, Attorney General (AG) Richard Blumenthal advised the agency to only continue to pay the rate set forth in the old lease even if the state entered the holdover period. In view of the fact that the Konover Group would need the state's permission to institute legal action to enforce the holdover provision and based on the AG's letter, it is not clear whether double rent will be paid if no new agreement is signed by February 15, 2005.

2,042,000

State Employee Wage Increases - A range of \$5.5 million to \$21.4 million may need to be added to the FY 05 budget depending upon whether a 1 year wage freeze is extended or not to 6 contracts which have expired as of 6/30/03 and 6/30/04 and remain unsettled. Ten more contracts (that have not agreed to a wage freeze) will expire 6/30/05 and 1 on 6/30/06. Preliminary estimates indicate that the cost of providing no wage freeze versus providing a 1 year wage freeze could approximate \$124.5 million cumulatively for all of these 17 unsettled contracts over the period of FY 05 through FY 07.

The amounts of \$62.7 million in FY 04 and \$126.1 million in FY 05 were removed from agency budgets in the original biennial budget for wage increases for contracts unsettled as of FY 03 through FY 05. During the 2004 session, \$48.4 million was appropriated in FY 04 and carried forward into FY 05 for certain contracts that subsequently became settled.

Nine contracts/arbitration awards approved during the 2004 session. Each includes a 1-year freeze on General Wage Increases (GWI's) and Annual Increments (AI's) with the following exceptions: 1) the Corrections Supervisors unit has no GWI or AI freeze and 2) the Social and Human Services unit has a GWI freeze, but no AI freeze. More than half of all state employees will have experienced a 1-year wage freeze by FY 05, when the employees subject to a wage freeze in the 2004 contract/arbitration awards are added to the higher education employees who agreed to a wage freeze during the 2003 session and the state managers who experienced a wage freeze in FY 03.

5,500,000 21,400,000

II. FY 06 and FY 07 General Fund Budget Projections

Our current services analysis indicates potential General Fund shortfalls of \$672.6 million in FY 06 and \$859.6 million in FY 07. These amounts are higher (by \$68.8 million in FY 06 and \$158.2 million in FY 07) than our November 12, 2004 projections of \$603.8 million in FY 06 and \$701.4 million in FY 07 largely because subsequently received actuarial valuations for the state employee and teachers' retirement systems indicated the need for additional funding of \$158.5 million in FY 06 and \$166.8 million in FY 07. Revised revenue projections, which are higher by \$83 million in FY 06 and \$26 million in FY 07, partially offset the expenditure increases. Current services expenditures would exceed the spending cap in both years by \$515.8 million or \$650 million in FY 06 and by \$754.6 million or \$893.7 in FY 07 with the lower numbers assuming that appropriations are increased to the allowable cap level in FY 05.

The shortfalls in these years are attributable to: 1) unavailable one-time revenues and tax changes together totaling \$508.4 million; and 2) expenditure growth which is anticipated to exceed revenue growth.

The projections in this report are based on present law, existing policy commitments, estimated caseload and workload requirements. The FY 06 and FY 07 figures are also based on using FY 05 as the baseline for revenue and expenditure projections and assume modest growth in the state and national economy. These estimates show the direction of revenues and spending if current laws and policies remain unchanged. They are not forecasts of what will actually occur, since policymakers will likely seek to alter current priorities.

FY 06 and FY 07 Revenues

The FY 06 revenue projection of \$13,657.0 million represents a 4.0% increase over our FY 05 revised estimate after adjusting for FY 05 one-time revenues and tax and revenue changes beginning in FY 06. The FY 07 revenue projection of \$14,268.0 million represents a 4.2% increase over FY 06 after adjusting for tax and revenue changes beginning in FY 07. The FY 06 and FY 07 figures were developed using the FY 05 estimates less one-time revenue as the base. The projections assume modest economic growth over the next two and half years and no recession. Two exceptions to this assumption are projections for the Real Estate Conveyance Tax and Oil Companies Tax. These two sources have experienced historic growth over the last couple of years that is not likely to be sustained over the next biennium. Therefore, the estimates for these two sources assume a decline in revenue.

FY 06 and FY 07 Expenditures

The FY 06 General Fund expenditure projection of \$14,329.6 million represents a \$930.5 million or 6.9% (adjusted) increase over FY 05 and the FY 07 projection of \$15,127.6 million represents a \$798 million or 5.6% increase over FY 06. This projection has been developed by applying inflationary guidelines and other specific

growth factors to the FY 05 estimated expenditure level. The guidelines utilized assume a one year wage freeze for unsettled contracts and reflect 4.5% salary increases for state employees in subsequent years (which includes 3% for cost of living adjustments and 1.5% for Annual Increments) and 2% in each year for other accounts; however, each major appropriated account has been examined individually and adjusted as necessary to reflect amounts anticipated to be required based on present law and caseload projections.

Several accounts with major FY 06 and FY 07 increases include:

Major General Fund Increases for FY 06 and FY 07 as of January 28, 2005 (figures in \$ millions)

	FY 06	FY 07
Teachers' Retirement Contributions	210.9	15.8
DSS – Medicaid	193.8	206.5
State Employee Retirement Contributions	92.8	30.0
SDE – Excess Cost-Student Based	56.4	17.2
Debt Service	50.1	106.4
Generally Accepted Accounting Principles (GAAP)	<u>39.0</u>	<u>56.2</u>
Total – Major General Fund Increases	643.0	432.1

The increases for Teachers' Retirement Contributions indicated above allow 100% funding of normal cost plus 40-year amortization of unfunded liabilities in accordance with current law.

Implementation of Generally Accepted Accounting Principles (GAAP) is scheduled to begin on July 1, 2005 under current law. Our projections include the impact of the conversion to GAAP in FY 06, which adds approximately \$39 million to the budget on a net expenditure basis in that year and annualizes to approximately \$95.2 million including amortization of the GAAP deficit in each of the following 15 fiscal years. The Comptroller's monthly report dated January 3, 2005 indicates that the cumulative General Fund GAAP deficit as of June 30, 2003 was \$842.3 million and anticipates updating the GAAP deficit in February of 2005.

III. Transportation Fund

FY 05

The FY 05 Transportation Fund operating deficit is projected to be \$2.3 million, which is \$5.4 million less than estimated previously. The un-audited cumulative surplus figure for the fund at the end of FY 04 is \$132.1 million and the cumulative surplus at the end of FY 05 is now projected to be \$129.9 million. The revised figures reflect the transfer of \$31.0 million from the Transportation Fund to the Transportation Strategy Board (TSB) projects account. Revised net expenditures reflect \$2.9 million in savings from the Governor's January 14th announcement of a statewide hiring freeze as well as \$4.5 million in savings from reduced Debt Service costs. The savings is offset by \$2.6 million in increased snow and ice removal expenditures associated with recent snow storms.

FY 06 and FY 07

OFA's FY 06 and FY 07 projections show deficits in both years as a result of two main factors. First, in each fiscal year there is a \$25 million reduction in the amount of Oil Companies Tax transferred from the General Fund to the Transportation Fund (PA 02-1.) Second, the growth rate in expenditures is predicted to outpace revenue growth in both years.

Projections of FY 06 anticipate that growth in expenditures will be 5.6%, much greater than the 3.3% growth rate for transportation revenues. For FY 07 the growth in expenditures exceed growth in revenues by 0.3%. The growth in expenditures is anticipated to be 3% whereas revenues are expected to grow by 2.7% for FY 07. Significant on-going expenditures affecting overall growth factors are presented below.

The two major factors responsible for the overall growth in Transportation Fund are DOT and DMV expenditures. OFA's projections for DOT's current services expenditures in FY 06 and FY 07 are 5.8% and 5.0%, respectively, over FY 05 appropriations. These substantial growth rates are primarily due to:

- unfunded accumulated leave:
- anticipated growth in overtime requests, primarily for snow and ice removal;
- increased fuel and heating oil costs due to market price increases;
- increased rail and bus operation deficits due to economic conditions and the impact of September 11, 2001;
- increase in expenditures for DOTs Handicapped Access Program. The program is an unfunded federal mandate that requires the state to provide on-demand service for areas within ¾ mile of a fixed bus route service. Historically, this program has been under funded;
- the DMV Vision Screening Program scheduled to be implemented increases total expenditures in the Transportation Fund by \$1.1 million in FY 06 and FY 07.

Also impacting FY 06 growth in expenditures is one-time \$10 million expenditure for completion of DMV's Real Time Online (RTOL) system. In FY 05 \$15.5 million has already been spent on this program funded through from combined lapse savings from Debt Service and DOT's personnel services.

FY 08 and Out Years

Out year projections indicate that the Transportation Fund will continue to experience operating deficits each year, which will completely eliminate the cumulative surplus by FY 09. This is attributable to the combined effects of the on-going annual loss of \$25 million in transfers

(PA 02-1) from the General Fund's Oil Companies Tax coupled with the expectation that growth in expenditures will exceed growth in revenues.

FY 05 Transportation Fund Summary as of January 28, 2005 (in millions)

Revenues	Budget <u>Plan</u>	Increase (Decrease)	Revised Estimates
Reveilues			
Taxes Other Revenue (incl. Refunds of Payments and Transfers) Total Revenue	545.3 399.3 944.6	2.0 -25.0 -23.0	547.3 374.3 921.6
Appropriations			
Appropriations - Gross	940.3	-5.4	934.9
Less: Lapse	-11.0	0.0	-11.0
Total Expenditures	929.3	-5.4	923.9
Surplus/(Deficit) from Operations for FY 05	15.3	-17.6	-2.3
Plus: Cumulative Surplus as of June 30, 2004	116.5	15.6	132.1
Projected Fund Balance as of June 30, 2005	131.8	-2.0	129.9

FY 05 Transportation Fund Revenues as of January 28, 2005 (in millions)

	Budget Plan	Increase (Decrease)	Revised Estimates
TAXES	<u> </u>	(Decircuse)	Lotimates
Motor Fuels Tax Petroleum Products Tax Sales Tax - DMV Refund of Taxes	471.0 13.0 70.0 -8.7	0.0 0.0 2.0 0.0	471.0 13.0 72.0 -8.7
Total - Taxes less Refunds	545.3	2.0	547.3
OTHER SOURCES			
Motor Vehicle Receipts License, Permits and Fees Interest Income Federal Grants (FTA) Transfers to Other Funds	226.2 159.1 27.0 3.3 -8.5	3.8 0.0 0.0 -2.8 0.0	230.0 159.1 27.0 0.5 -8.5
Total - Other Sources	407.1	1.0	408.1
Less Refunds of Payments Less Transfers to TSB Account	-2.8 -5.0	0.0 -26.0	-2.8 -31.0
TOTAL REVENUE	944.6	-23.0	921.6

Transportation Fund Projections FY 05 - FY 10 as of January 28, 2005 (in millions)

Transportation Fund	FY 05	FY 06	FY 07	FY 08	FY 09	FY 10
Beginning Balance as of July 1st	,	(Estimated) \$129.9	(Estimated) \$105.3	(Estimated) \$77.3	(Estimated) \$29.3	(Estimated) (\$36.9)
beginning balance as or only 1st	(Un-audited)	Ψ123.3	ψ100.0	Ψ11.5	Ψ23.0	(ψου.ο)
REVENUES	(On-addited)					
Taxes						
Motor Fuels Tax	471.0	478.6	485.6	492.6	500.0	507.2
Petroleum Products Tax	13.0	21.0	21.0	21.0	21.0	21.0
Sales Tax - DMV	72.0	74.0	76.0	78.0	80.0	81.0
Refund of Taxes	(8.7)	(8.6)	(8.8)	(9.0)	(9.0)	(9.2)
Total - Taxes less Refunds		\$565.0	\$5 7 3.8	\$5 82. 6	\$5 92. 0	\$600.0
Other Revenue Sources						
Motor Vehicle Receipts	230.0	236.9	244.0	251.3	255.1	262.7
License, Permits and Fees	159.1	161.3	163.5	165.8	168.1	170.0
Interest Income	27.0	29.0	32.0	33.0	34.0	34.0
Federal Grants (FTA)	0.5	0.5	0.5	0.5	0.5	0.5
Transfers to Other Funds	(8.5)	(8.5)	(8.5)	(8.5)	(8.5)	(8.5)
Release from Debt Service Reserves	0.0	0.0	0.0	0.0	0.0	0.0
Total - Other Sources	\$408.1	\$419.2	\$431.5	\$442.1	\$449.2	\$458.7
Less Refunds of Payments	(2.8)	(2.8)	(2.8)	(2.8)	(2.8)	(2.8)
Less Transfers to TSB Account (1)	(31.0)	(29.3)	(24.3)	(24.3)	(24.3)	(24.3)
TOTAL REVENUE	\$921.6	\$952.1	\$978.2	\$997.6	\$1,014.1	\$1,031.6
EXPENDITURES						
Debt Service	418.4	430.3	434.6	438.0	435.6	433.5
DOT Budgeted Expenses	371.8	390.4	407.6	425.5	444.3	463.8
DMV Budgeted Expenses	50.5	62.7	55.0	57.5	60.0	62.3
Other Budgeted Expenses	94.2	104.2	119.9	135.7	151.4	167.2
Subtotal - Expenditures	\$934.9	\$987.6	\$1,017.2	\$1,056.7	\$1,091.3	\$1,127.1
Less Unallocated Lapses	(11.0)	(11.0)	(11.0)	(11.0)	(11.0)	(11.0)
TOTAL EXPENDITURES	\$923.9	\$976.6	\$1,006.2	\$1,045.6	\$1,080.3	\$1,116.1
OPERATING SURPLUS/(DEFICIT)	(\$2.3)	(\$24.5)	(\$28.0)	(\$48.0)	(\$66.2)	(\$84.5)
Ending Balance as of June 30th	\$129.9	\$105.3	\$77.3	\$29.3	(\$36.9)	(\$121.4)
DEBT SERVICE RATIO(2)	2.3	2.3	2.3	2.3	2.4	2.4

⁽¹⁾ Incremental revenue from the various DMV fee changes allocated to the Transportation Strategy Board (TSB) and deposited in the TSB projects account.

⁽²⁾ Pledged revenues for reserves required under the Indentures in an amount at least two (2) times the aggregate Principal and Interest Requirements on all outstanding Bonds and Notes.